Supreme Court, U. S.
FILED
FEB 10 1975
MICHAEL RODAK, JR., CLERK

No. 74-996

In the Supreme Court of the United States

OCTOBER TERM, 1974

UNITED STATES OF AMERICA, PETITIONER

v.

DATA PRODUCTS CORPORATION

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

ROBERT H. BORK,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

In the Supreme Court of the United States

OCTOBER TERM, 1974

No.

UNITED STATES OF AMERICA, PETITIONER

v.

DATA PRODUCTS CORPORATION

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

The Solicitor General, on behalf of the United States of America, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit in this case.[1]

OPINIONS BELOW

The judgment of the district court (Appendix A, *infra*) is not officially reported. The order of affirmance of the court of appeals (Appendix B, *infra*) is not reported.

JURISDICTION

The judgment of the court of appeals was entered on December 27, 1974 (Appendix C, *infra*). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

---

[1]Although respondent was the succesful party below, it has filed a petition for a writ of certiorari (No. 74-854) to review the decision of the court of appeals. We are filing simultaneously with this petition a memorandum in opposition to respondent's petition.

QUESTION PRESENTED

Section 172 of the Internal Revenue Code of 1954 permits the carryback of a net operating loss to a taxable year prior to the year in which the loss is sustained, and a carryover to a succeeding year of the amount, if any, by which the loss exceeds the taxable income for each prior year to which the loss may be carried.

The question presented is whether, in carrying back a net operating loss to a year in which the taxpayer had both ordinary income and capital gains and employed the alternative tax computation method of Section 1201, the loss deduction available for carryover to a succeeding year is the amount by which the loss exceeds only the ordinary income for the prior year, as the decision below held, or the amount by which the loss exceeds both the ordinary income and capital gains for the prior year.

STATUTES INVOLVED

The relevant portions of Sections 172 and 1201 of the Internal Revenue Code of 1954 are set forth in Appendix D of the petition for a writ of certiorari in *United States* v. *Foster Lumber Company, Inc.*, No. 74-799.

STATEMENT

For its taxable years ended March 31, 1968 through 1971, respondent reported the following amounts of ordinary and capital gains income:[2]

[2]In granting the judgment for respondent, the district court did not make any findings of fact. The court of appeals summarily affirmed prior to the filing of briefs or a record appendix. Accordingly, the Statement is based on the undisputed facts as set forth in the original record.

Taxable Year	Net Ordinary Income	Excess of Net Long-Term Capital Gain Over Net Short-Term Capital Loss	Total Taxable Income
1968	$2,683,774	_____	$ 2,683,774
1969	$ 560,746	$18,095,643	$18,656,389
1970	$ 662,604	_____	$ 662,604
1971	($8,818,189)	_____	($ 8,818,189)

Because respondent sustained a net operating loss of $8,818,189 for its taxable year 1971, it elected to carry back that loss to 1968, and filed a Form 1139 (Corporation Application for Tentative Refund from Carryback of Net Operating Loss). That carryback resulted in the complete offset of respondent's 1968 taxable income, leaving a net operating loss of $6,134,415 available to be carried over to 1969. As the Code prescribes, respondent recomputed its 1969 tax liability under both the method provided by Section 11 (the so-called "regular method"), and the "alternative tax computation method" provided by Section 1201 of the Code. Taking into account the carryback of its 1971 losses in the amount of $6,134,415, respondent's computations of its 1969 income tax liability under each of the two methods were as follows:

"Regular Method" (Section 11)

Taxable Income (excluding net operating loss deduction):		
Ordinary income	$ 560,746	
Capital gains income	18,095,643	$18,656,389
LESS: Net operating losses deduction resulting from carryback of 1971 net operating loss		6,134,415

Taxable Income (Section 63(a))		$12,521,974
Regular tax (1969 rates)		$ 6,003,548

"Alternative Method" (Section 1201)

Taxable Income (excluding net operating loss deduction):		
Ordinary income	$ 560,746	
Capital gains income	18,095,643	$18,656,389
LESS: Net operating loss deduction resulting from carryback of 1971 net operating loss		6,134,415
Taxable Income (Section 63(a))		$12,521,974
(Step 1 - Partial Tax)		
LESS: Excess of net long-term capital gain over net short-term capital loss		18,095,643
Balance		($ 5,573,669)
Partial Tax at Section 11 rates on balance (Section 1201(a)(1))		- 0 -
(Step 2 - Capital Gains Tax)		
PLUS: Capital Gains Tax at flat 25 percent rate on excess of net long-term capital gain over net short-term capital loss (Section 1201(a)-(2))		4,523,911
Alternative Tax (1969 rates)		$ 4,523,911

Since the $4,523,911 tax computed under the "alternative method" of Section 1201 was lower than the tax computed under the "regular method" of Section 11, respondent was required to and did report the amount of the alternative tax computed under the provisions of Section 1201 as its recomputed 1969 tax liability.

This suit involves respondent's tax liability for its taxable year ended March 31, 1970. In applying for a tentative refund from the carryover of its 1971 net operating loss to that year, respondent claimed that $5,573,669 of its 1971 loss of $8,818,189, which had been first carried back to 1968 (reducing the loss to $6,134,415), and then to 1969, was available to offset income for 1970. Respondent based its claim on the contention that its 1971 loss had been reduced in 1969 only to the extent of its ordinary income of $560,746 for that year.

On audit, the Commissioner of Internal Revenue disallowed respondent's claim for refund for its taxable year 1970. The Commissioner's disallowance was premised on the ground that respondent's 1971 net operating loss of $8,818,189 had been entirely "used" in computing its 1968 and 1969 taxable income in the respective amounts of $2,683,774 and $18,656,389. As a result, the Commissioner determined that no part of the 1971 net operating loss deduction remained available to respondent for its taxable year 1970.

The district court upheld respondent's claim for refund (Appendix A, *infra*), and the court of appeals summarily affirmed (Appendix B, *infra*).

REASONS FOR GRANTING THE WRIT

This case presents the identical issue as *United States* v. *Foster Lumber Company, Inc.*, 500 F.2d 1230 (C.A. 8), petition for a writ of certiorari pending, No. 74-799.

For the reasons stated in our petition for a writ of certiorari in *Foster Lumber*, a copy of which we are furnishing to respondent's counsel, the decision below is in square conflict with *Mutual Assurance Society of Virginia Corp.* v. *Commissioner*, 505 F.2d 128 (C.A. 4), and rests upon an erroneous interpretation of the term "taxable income" as it is employed in Section 172(b)(2). That term is defined by Section 63(a) of the Code as gross income less allowable deductions. The court of appeals' conclusion that respondent's 1971 carryback loss was offset only to the extent of its ordinary income for 1968 and 1969 flatly contradicts the definition of that term in Section 63(a).

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

ROBERT H. BORK,
Solicitor General.

FEBRUARY 1975.

APPENDIX A

UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA

No. CV 74-238-AAH

DATA PRODUCTS CORPORATION, PLAINTIFF

v.

UNITED STATES OF AMERICA, DEFENDANT

JUDGMENT

Plaintiff having filed a motion for summary judgment and the Court having been fully advised in the premises and having made and entered its Findings of Fact and Conclusions of Law herein;

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that the Plaintiff recover from the Defendant the amount of $152,451, together with interest as provided by law and that there be assessed against Defendant all costs as provided by law.

Dated this 25th day of September, 1974.

A. Andrews
UNITED STATES DISTRICT JUDGE

APPENDIX B

DATA PRODUCTS CORPORATION,

Plaintiff-Appellee,

No. 74-3341

vs.

ORDER

UNITED STATES OF AMERICA,

Defendant-Appellant.

Before: TRASK and GOODWIN, Circuit Judges

The judgment of the district court entered September 25, 1974 is hereby affirmed. *Olympic Foundry Company* v. *United States*, 493 F.2d 1247 (9th Cir. 1974).

Filed December 27, 1974

/s/ Ozell M. Trask

/s/ Alfred T. Goodwin

APPENDIX C

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

DATA PRODUCTS CORPORATION,

Plaintiff-Appellee

v. 74-3341

UNITED STATES OF AMERICA,

Defendant-Appellant

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA

JUDGMENT

THIS CAUSE came on to be heard on the transcript record from the United States District Court for the Central District of California

and duly submitted.

ON CONSIDERATION WHEREOF, it is now here ordered and adjudged by this Court, that the judgment of the said District Court, in this cause, be, and the same hereby is, affirmed.

Filed and entered December 27, 1974.

[SEAL]

A true copy:

Attest: /s/ Emil E. Melfi, Jr.,

Clerk, U.S. Court of Appeals, 9th Circuit.

Supreme Court, U. S.
FILED
MAR 11 1975
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

October Term, 1974
No. 74-996

UNITED STATES OF AMERICA,

Petitioner,

vs.

DATA PRODUCTS CORPORATION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

BRIEF OF THE RESPONDENT IN OPPOSITION.

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IN THE

Supreme Court of the United States

October Term, 1974
No. 74-996

UNITED STATES OF AMERICA,

Petitioner,

vs.

DATA PRODUCTS CORPORATION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

BRIEF OF THE RESPONDENT IN OPPOSITION.

The Respondent, Data Products Corporation, opposes the granting of the petition for a writ of certiorari filed on behalf of the United States of America to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in this case.

Question Presented.

The taxpayer corporation incurred a net operating loss in the year 1971. In accordance with I.R.C. Section 172(b), a portion of the loss served as a deduction to reduce the corporate income tax on its ordinary business income earned in 1968 and 1969. During the year 1969, the taxpayer also had a capital gain, the tax on which was determined under the so-called alternative tax imposed by I.R.C. Section 1201(a) on corporate capital gains; no part of the 1971 net operat-

ing loss served to reduce the tax on the taxpayer's 1969 capital gains.

The question is whether the Court below was correct in concluding that the portion of the 1971 loss, not deductible in prior years and not deductible in computing the 1969 tax on capital gains, was still available as a deduction against the corporation's 1970 ordinary net income.

Statutes Involved.

The pertinent statutory provisions involved are set forth in Appendix A, *infra*.

Statement.

During its taxable year ended March 27, 1971, Petitioner incurred a net operating loss which, as finally agreed to between it and the Commissioner of Internal Revenue, was $8,818,189.00.[1] For its taxable year ended March 30, 1968, $2,683,774.00 of such loss served as a deduction against Petitioner's net ordinary income for such year in accordance with the provisions of I.R.C. Section 172(b), and $560,746.00 of

[1]The Statement of the case of Respondent contains a summary of the relevant portions of the Findings of Fact and Conclusions of Law of the District Court. Such findings of fact were based on the pleadings of the parties, and on no other evidence, the District Court having granted a Motion for Summary Judgment based on such pleadings.

The Statement of the Case set forth in the Petition of the United States has obviously not been prepared from the record in this case (and in fact contains errors even if it purported to be a summary of the administrative files of the Internal Revenue Service). It also erroneously states in footnote 2, that the District Court did not make any findings of fact, and that the statement of the United States is based on the undisputed facts set forth in the original record. While the Solicitor General, by letter to the Clerk of the Court, has called attention to this error, for the convenience of the Court, we are setting forth, in Appendix B, the Findings of Fact and Conclusions of Law of the District Court.

such loss similarly served as a deduction against net ordinary income for the year ended March 29, 1969. During the year ended March 29, 1969, the Petitioner also had a capital gain, the tax on which was computed under I.R.C. Section 1201(a), the so-called alternative tax on corporate capital gains.

For the year ended March 28, 1970, the year in issue, the United States District Court held that since only a portion of the 1971 loss was utilizable as a deduction against the taxpayer's ordinary net income in the years 1968 and 1969, the balance of the 1971 net operating loss was available as a deduction in the year 1970 and the still unused portion in future years. It rejected the contention of the United States that the balance of the 1971 loss was utilized in 1969 (and hence not available in 1970) against the capital gains of that year, on the evident thesis that, since the 1969 capital gain was taxable under the so-called alternative tax imposed by I.R.C. Section 1201(a), and the amount of the tax on such capital gains was not diminished or affected by the 1971 loss, the balance of the 1971 loss had not been utilized as a deduction in 1969. Accordingly, it granted summary judgment for the Petitioner on the authority of *Olympic Foundry Co., Inc. v. United States,* 493 F.2d 1247 (9th Cir. 1974).

The Court of Appeals, on the Petitioner's motion, summarily affirmed the judgment of the District Court on the authority of its own prior decision in *Olympic Foundry Co., Inc. v. United States, supra.*[2]

[2]The Respondent herein has previously filed a Petition (Docket No. 74-854) for a Writ of Certiorari in this case stating, in effect, that the Petition should be granted only in the event that the Petition of the United States in *Foster Lumber Co.* is granted.

(This footnote is continued on next page)

REASONS WHY THE PETITION FOR A WRIT OF CERTIORARI SHOULD BE DENIED.

1. It is doubtful whether the question presented in this case, and in the companion case of *United States v. Foster Lumber Co., Inc.* (Docket No. 74-799), both of which represent harmonious decisions, and in both of which the United States has filed Petitions, is of sufficient importance to warrant review by this Court, even though there is a seeming conflict arising out of the decision of the Fourth Circuit, decided by a divided Court, in *Mutual Assurance Society of Virginia Corp. v. Commissioner,* 505 F.2d 128 (C.A. 4th 1974), a case which is not pending in this Court, no Petition for a Writ of Certiorari having been filed in that case.

There is, according to the petition filed by the United States in *Foster Lumber Co.,* only some thirty million dollars of revenue involved arising out of the returns of 164 corporations being considered at the administrative level where the same kind of problem is at issue. For all that is known, none of these corporate taxpayers are within the jurisdiction of the Court of Appeals for the Fourth Circuit, the only Court which has agreed with the views of the United States, and these taxpayers may be subject to the jurisdiction of the Courts of Appeals which have rejected those views (namely, the First, Eighth and Ninth Circuits) or of

The Petition had the purpose of permitting this Court to determine whether review should be granted in this case at the same time when it considered the *Foster Lumber Co.* petition.

Since the United States has now filed its petition in this case, and since the Court will consider the petitions of the United States in the *Foster Lumber Co.* case and in this case together, we have stipulated with the Solicitor General that the Petition in Docket No. 74-854 be dismissed.

those Courts of Appeals which have not yet considered the problem.

Further, on another, but full presentation of the issue, the Fourth Circuit, which is itself divided on the issue, may alter its views. That is, the amount of tax at issue in the *Mutual Assurance* case, *supra,* was so small that the taxpayer there did not see fit to seek review by this Court and permitted the adverse judgment to become final. In the event that a future case should arise in that jurisdiction, affecting a taxpayer whose financial involvement permits a full presentation of the issue, that Court may reconsider its position, remove the present division in that Court, join the other Courts of Appeals which have spoken on the question, and leave the state of the law harmonious, without the need for intervention by this Court.

2. The relatively small amount of revenue which would be affected by this issue should be balanced against the fairly complex problems which would have to be considered by this Court if it were to review the present cases against the backdrop of the opposing views of the Fourth Circuit.

That is, prior to the decision in *Mutual Assurance Society of Virginia, supra,* the unanimous decisions of the Tax Court[3] and of the First,[4] Eighth[5] and Ninth Circuits[6] involved a fairly simple question of the proper

[3] *Chartier Real Estate Co. v. Commissioner,* 52 T.C. 346 (1969). The Tax Court has repeatedly followed this decision in all subsequent cases.

[4] *Chartier Real Estate Co. v. Commissioner,* 428 F.2d 474 (1970), affirming the decision of the Tax Court cited in footnote 3.

[5] *United States v. Foster Lumber Co.,* 500 F.2d 1230 (1974), pending on petition for a writ of certiorari (Docket No. 74-799).

[6] *Olympic Foundry Company v. United States,* 493 F.2d 1247 (1974), and the present case.

interpretation of the loss carry-over provisions of Code Section 172(b) and of the so-called alternative tax for corporations provided for in Code Section 1201. Both provisions are in Appendix A, *infra*. The Fourth Circuit, however, in *Mutual Assurance Society of Virginia, supra,* turned this rather simple question into a fairly complex one, for its rationale is largely grounded on the proposition, erroneous, we contend, that the Congressional policy for taxing capital gains to individual taxpayers is precisely the same as it is for corporate taxpayers; based on that premise, and on other considerations, it concluded that the loss carry-over provisions were intended by Congress to operate precisely the same for both individual and corporate taxpayers.

(a) Although the capital gain and loss provisions of Sections 1201, 1202, 1211 and 1212 each contain provisions which are separately applicable to corporations and to other taxpayers (which is the first indication of why the Fourth Circuit's rationale is wrong), a full consideration of that proposition would require not only a complete examination of the entire history of the capital gains provisions and the net operating loss provisions of the taxing statute, but also, as shown below, an examination of a goodly portion of the entire Internal Revenue Code.

(b) Since Congress has always seen fit to tax a corporation as a separate entity, Congress was required to enact provisions, constantly growing in ever increasing complexity, which would attempt to separate the ordinary income tax consequences from the capital gain treatment with which a stockholder should be taxed and to attempt to close "loop holes" at both the corporate as well as the stockholder level. We list only some of these provisions of the Internal Revenue Code:

Sections 301, 302, 303, 304, 305, 311, 312, 316, 318, 331, 332, 334, 341, 522-537, 542-557. A full discussion of these sections, and others, their interplay with each other, and of a substantial portion of the fabric of the taxing statute, while inappropriate for discussion at this time, would have to be considered by this Court if this case and the *Foster Lumber Co.* case were heard on their merits.

(c) The fact that neither an individual taxpayer nor his estate will pay a capital gains tax when death occurs, and that such a tax consequence is not available to a corporation, is another indication that the Congressional policy of taxing capital gains is not the same for both types of taxpayers.

(d) Again, while the kind of assets which will qualify for capital gain treatment is somewhat limited where a corporate taxpayer is involved (see *Corn Products Refining Co. v. Commissioner,* 350 U.S. 46 (1955)), broader definitions of a capital asset apply to non-business property held by an individual taxpayer.

These, and other considerations, would not need to be examined by this Court at this time, or possibly in the future, if the majority of the panel of the Fourth Circuit, which heard the *Mutual Assurance Society* case, were to reexamine and change its conclusions.

3. The decision below and that in *Foster Lumber Co.* are correct; the contrary interpretation reached by the Fourth Circuit is plainly wrong.

The loss carry-over provisions of Section 172 were designed to avoid the harsh burden of an annual accounting system where a corporate taxpayer has fluctuations in its earnings, with losses in some years and earnings in others, and to put it on a parity with the cor-

porate taxpayer which has a more steady earnings history, but where its overall results, measured over a period of time, are no different from those of the more erratic business. See H. Rep. No. 855, 76 Cong. 1st Sess.; 1939-2 Cum. Bull. 504, 510-511.

But the decision reached by the Fourth Circuit, when capital gains are involved, results in imposing a much greater tax burden on the corporation whose business is more volatile than it does with respect to the corporation whose earnings are steady. For example: Corporation A has $500,000 of capital gains as well as $600,000 of business income in year 1. It has business losses of $800,000 in year 2 and $800,000 of business income in year 3. Corporation B also has $500,000 of capital gains in year 1, and it has $200,000 of business income in that year, $200,000 of business income in year 2 and $200,000 of business income in year 3.

Taken over the 3 year period, the net results of operations of both corporations are the same; each has earned a total of $600,000 of ordinary business income and $500,000 of capital gains.

Under the decision of the Court below, the total taxes of each corporation for all 3 years would, except for the corporate surtax exemption, be precisely the same; they are actually $406,500 for Corporation A and $393,500 for Corporation B.[7]

[7]Under Section 11 of the Internal Revenue Code, the first $25,000 of corporate income is taxed at the rate of 22 percent and all income in excess of that (except where the alternate tax on capital gains is involved) is taxed at 48 percent. The $13,000 of difference in tax between Corporation A and Corporation B in the example is attributable solely to this rate "bracket."

Under the decision of the Fourth Circuit, the total taxes of Corporation A would be $502,500, while the total taxes of Corporation B would be only $393,500 thus penalizing Corporation A and its volatile earnings.

This difference in tax cost to the two corporations arises from the Fourth Circuit's conclusion that A's portion of its business losses in year 2, not utilized against its business income of year 1, namely, the excess of $200,000, is not available to diminish its taxable business income in year 3 on the theory that such excess was utilized against the capital gain income of year 1, *even though the tax on the capital gain income of year 1 was not diminished or otherwise affected by the business loss of year 2, and no tax benefit resulted from the existence of the loss.* The decision of the Court below and that of the other harmonious Courts is to the effect that the excess is available to reduce the taxable business income of year 3 from $800,000 to $600,000 since the $200,000 was not available to reduce the capital gains tax in year 1, thus bringing the tax burden on both corporations into parity.

It is submitted that the conclusion of the Court below is in accord with the Congressional intendment, while that of the Fourth Circuit is at war with the Congressional policy and should be rejected.

Conclusion.

For the reasons stated above, the petition of the United States for a writ of certiorari should be denied.

Respectfully submitted,

HILBERT P. ZARKY,
Counsel for Respondent.

Of Counsel:
MITCHELL, SILBERBERG & KNUPP,

APPENDIX A.

Internal Revenue Code of 1954 (26 U.S.C.).

Sec. 172. Net Operating Loss Deduction.

(a) *Deduction Allowed.*—There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term "net operating loss deduction" means the deduction allowed by this subsection.

(b) [as amended by Sec. 317(b), 76 Stat. 872]

Net Operating Loss Carrybacks and Carryovers.—

(1) *Years to which loss may be carried.*—

(A) (i) [as amended by Sec. 210(a)(1), Revenue Act of 1964, P.L. 88-272, 78 Stat. 19, Sec. 3(a)(1), Act of December 27, 1967, P.L. 90-225, 81 Stat. 730, and Sec. 431(b), Tax Reform Act of 1969, P.L. 91-172, 83 Stat. 487]. Except as provided in clause (ii) and subparagraphs (D), (E), (F) and (G), a net operating loss for any taxable year ending after December 31, 1957, shall be a net operating loss carryback to each of the 3 taxable years preceding the taxable year of such loss.

(B) Except as provided in subparagraphs (C), (D), and (E), a net operating loss for any taxable year ending after December 31, 1955, shall be a net operating loss carryover to each of the 5 taxable years following the taxable year of such loss.

(2) *Amount of carrybacks and carryovers.*— Except as provided in subsections (i) and (j), the entire amount of the net operating loss for any taxable year (hereinafter in this section referred to as the "loss year") shall be carried to the earliest of the taxable years to which (by reason of paragraph (1)) such loss may be carried. The portion of such loss which shall be carried to each of the other taxable years shall be the excess, if any, of the amount of such loss over the sum of the taxable income for each of the prior taxable years to which such loss may be carried. For purposes of the preceding sentence, the taxable income for any such prior taxable year shall be computed—

(A) with the modifications specified in subsection (d) other than paragraphs (1), (4), and (6) thereof; and

(B) [as amended by Sec. 210(b)(1) and (2), Revenue Act of 1964, *supra*] by determining the amount of the net operating loss deduction—

(i) without regard to the net operating loss for the loss year or for any taxable year thereafter, and

(ii) without regard to that portion, if any, of a net operating loss for a taxable year attributable to a foreign expropriation loss, if such portion may not, under paragraph (1)(D), be carried back to such prior taxable year,

and the taxable income so computed shall not be considered to be less than zero.

Sec. 1201. Alternative Tax.

(a) [as amended by Sec. 8(g)(3), Revenue Act of 1962, P.L. 87-834, 76 Stat. 960] *Corporations.*— If for any taxable year the net long-term capital gain of any corporation exceeds the net short-term capital loss, then, in lieu of the tax imposed by sections 11, 511, 821(a) or (c), and 831(a), there is hereby imposed a tax (if such tax is less than the tax imposed by such sections) which shall consist of the sum of—

(1) a partial tax computed on the taxable income reduced by the amount of such excess, at the rates and in the manner as if this subsection had not been enacted, and

(2) an amount equal to 25 percent of such excess, or, in the case of a taxable year beginning before April 1, 1954, an amount equal to 26 percent of such excess.

In the case of a taxable year beginning before April 1, 1954, the amount under paragraph (2) shall be determined without regard to section 21 (relating to effect of change of tax rates).

APPENDIX B.

Findings of Fact and Conclusions of Law. (Revised)

United States District Court, Central District of California.

Data Products Corporation, Plaintiff, v. United States of America, Defendant. No. CV 74-238-AAH.

Plaintiff having filed a Motion for Summary Judgment and the Court being fully advised in the premises makes the following findings of fact and conclusions of law.

FINDINGS OF FACT

1. The Plaintiff is a corporation, organized under the laws of the State of Delaware, having its principal office at 6219 DeSoto Avenue, Woodland Hills, California 91364.

2. The Defendant is the United States of America.

3. Plaintiff, by its complaint, seeks the recovery of corporate income taxes for the year ended March 28, 1970 in the amount of $152,451.00, as having been erroneously paid to and illegally and erroneously assessed and collected by the Defendant, together with statutory interest thereon.

4. A claim for refund for the corporate taxes referred to in Paragraph 3 above was duly filed by Plaintiff with the Internal Revenue Service Center, 5045 East Butler Avenue, Fresno, California on January 5, 1973.

5. More than six months elapsed since the filing of the claim for refund referred to in Paragraph 4 above prior to the bringing of this action. Such claim for refund has neither been rejected nor otherwise acted

on by the Commissioner of Internal Revenue, or any of his authorized delegates.

6. The jurisdiction of this Court rests on U.S.C. Title 28, Sections 1340 and 1346(a)(1).

7. For its year ended March 28, 1971, Plaintiff reported on its tax return a net operating loss in the amount of $8,650,358.00, which loss has been increased to $8,818,189.00 by the Internal Revenue Service. In accordance with the provisions of Section 172(b), Internal Revenue Code of 1954, as amended (U.S.C. Title 26, Section 172(b)), $2,683,774.00 of said operating loss was utilizable, as a loss carryback, against Plaintiff's ordinary net income for the year ended March 30, 1968 and $560,746.00 of said loss was similarly utilizable, as a loss carryback, against its ordinary net income for the year ended March 29, 1969. During the year ended March 29, 1969, Plaintiff also had a capital gain, the tax on which was required to be computed under Section 1201, Internal Revenue Code of 1954, as amended (Title 26, Section 1201); no part of the loss carryback was used or utilizable in computing the tax on such capital gain.

8. For its taxable year ended March 28, 1970, prior to the application of any net operating loss carryback, the Plaintiff in its corporate income tax return reported taxable net income of $453,051.00 and a corporate income tax liability of $153,852.00. On or about July 5, 1974, the Commissioner of Internal Revenue determined that the Plaintiff had additional taxable income and assessed an additional corporate income tax in the amount of $165,677.00 for the year ended March 28, 1970, making a total tax liability of $319,529.00 for that year prior to the application of

any net operating loss carryback, which determination has been agreed to by the Plaintiff subject to the issues presented by this suit for refund which involves the proper applicability of Plaintiff's net operating loss carryback. Under Section 172(b), Internal Revenue Code of 1954, as amended (U.S.C. Title 26, Section 172(b)), Plaintiff was entitled to offset the unused portion of the net operating loss incurred during its year ended March 28, 1971 to the extent not carried back to its years ended March 30, 1968 and March 29, 1969 (which unused portion of the net operating loss carryback was $5,573,669) against its net taxable income for the year ended March 28, 1970 so that, except for investment credit recapture and minimum tax on preference items (the total tax liability on these items being in the amount of $1,401.00), it had no liability for corporate income taxes for such year.

9. Plaintiff has paid corporate income taxes, with respect to its taxable year ended March 28, 1970, in the amount of $910,000.00, such payment having been made in the amount of $100,000.00 on July 15, 1969, $100,000.00 on September 15, 1969, and $710,000.00 on March 13, 1970. Of such payment, there has been refunded to the Plaintiff the amount of $756,148.00. The Plaintiff has overpaid its corporate income taxes for the year ended March 28, 1970 in the amount of $152,451.00, which amount has been erroneously and illegally collected and assessed by the Commissioner of Internal Revenue, or his duly authorized delegates.

CONCLUSIONS OF LAW

1. The Plaintiff has erroneously paid and there has been illegally and erroneously collected from the Plaintiff corporate income taxes in the amount of $152,451.00 for the taxable year ended March 28, 1970.

2. The Plaintiff is entitled to summary judgment against the Defendant in the amount of $152,451.00, plus interest as provided by law.

3. Plaintiff is entitled to judgment for all assessable costs as provided by law.

4. To the extent that any of the findings of fact contain conclusions of law, they are incorporated herein.

5. There is no genuine issue of any material fact relative to the foregoing findings of fact.

Dated: Sept. 23, 1974

/s/ A. Andrew Hauk
United States District Judge
A. Andrew Hauk

Supreme Court, U. S.
FILED
MAR 17 1975

No. 74-996

In the Supreme Court of the United States

OCTOBER TERM, 1974

UNITED STATES OF AMERICA, PETITIONER

v.

DATA PRODUCTS CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

REPLY MEMORANDUM FOR THE UNITED STATES

ROBERT H. BORK,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

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Although respondent seemingly acknowledges (Br. Opp. 4, 7) the conflict between the decision below and that of the Fourth Circuit in *Mutual Assurance Society of Virginia Corp.* v. *Commissioner*, 505 F.2d 128, and the fact that at least $30 million of revenue is at stake, it nevertheless denies that the issue is sufficiently important to warrant review by this Court. But as we pointed out at page 11 of our petition for a writ of certiorari in *United States* v. *Foster Lumber Co.*, No. 74-799, which presents the identical issue, even the $30 million figure does not reflect additional amounts which are expected to arise as a result of the attempts of taxpayers to claim net operating loss carryover deductions for succeeding years on the ground that portions of such losses are still available to offset income.

That fact is dramatically illustrated by the pertinent figures in this case, where $152,451 is at stake for the taxable year in suit but an additional claimed loss carryover of $5 million is ultimately at issue. As respondent acknowledged at page 4 of its petition for a writ of certiorari in this case (No. 854), which has now been dismissed pursuant to stipulation, "it has an unused carryover in excess of $5,000,000.00 which will be available as a deduction in other taxable years if the decision below is affirmed but none of which would be so available if the views of the United States were ultimately to prevail." The question thus involves much more than $30 million of revenue.

Respondent further suggests (Br. Opp. 5, 6): (1) that the Fourth Circuit may alter its views in a subsequent case; and (2) that consideration of this question presented would require "an examination of a goodly portion of the entire Internal Revenue Code."

1. There is no basis for respondent's prediction that the Fourth Circuit may change its position in a subsequent case. Its decision in *Mutual Assurance Society of Virginia Corp.* v. *Commissioner, supra*, rendered just five months ago, is the most recent opinion of a court of appeals on the issue in which it expressly recognized the conflict and explicitly rejected the reasoning of both the Tax Court in *Chartier Real Estate Co.* v. *Commissioner*, 52 T.C. 346, 356-358, affirmed *per curiam*, 428 F.2d 474 (C.A. 1), and of the Eighth Circuit in *United States* v. *Foster Lumber Co.*, 500 F.2d 1230, petition for a writ of certiorari pending, No. 74-799.[1] More recently, the

[1]The opinions of the First and Ninth Circuits, which respondent (Br. Opp. 5) characterizes as "harmonious," are merely *per curiam* affirmances. *Chartier Real Estate Co.* v. *Commissioner*, 428 F.2d 474 (C.A. 1); *Olympic Foundry* v. *United States*, 493 F.2d 1247 (C.A. 9); and the decision below (Pet. App. B 2a).

Fourth's Circuit's views have been cited with approval by the Sixth Circuit in *Axelrod* v. *Commissioner*, No. 74-1511, decided December 17, 1974, reversing 32 T.C.M. 885 (decided August 25, 1973), a case involving the computation of a net operating loss of an individual taxpayer. There is accordingly a live conflict of decisions which only this Court can resolve.

2. Consideration of the question will not require "a complete examination of the entire history of the capital gains provisions and the net operating loss provisions of the taxing statute, [and] * * * an examination of a goodly portion of the entire Internal Revenue Code" (Br. Opp. 6). The issue is simply not that complicated or wide-ranging. It involves only the interplay between Section 172 of the Code, which provides for the carryback of a net operating loss, and Section 1201, the alternative tax computation for capital gains.

In upholding our position that a loss carryback is "used" by a taxpayer to the extent it offsets *both* the ordinary income and capital gains for the prior year rather than only the ordinary income for that year, the Fourth Circuit in *Mutual Assurance Society* construed the term "taxable income" in Section 172(b)(2) in conformity with its definition in Section 63(a), to include both ordinary income and capital gains (see 505 F.2d at 133-134). It is the meaning of that term in the loss carryback provision that is the issue in this case, and resolution of that issue does not require analysis of "a goodly portion of the entire Internal Revenue Code."

Respectfully submitted.

ROBERT H. BORK,
Solicitor General.

MARCH 1975.

DOJ-1975-03